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March 22, 2006

Mary F. Rupp, Esq.
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Re: Comments on Sixth EGRPRA Notice

Dear Ms. Rupp:

U.S. Central Federal Credit Union ("U.S. Central") appreciates the opportunity to respond to the National Credit Union Administration's (the "NCUA's") recent Notice of Regulatory Review and Request for Comments (the "Notice") pursuant to the Economic Growth and Regulatory Paperwork Reduction Action of 1996 ("EGRPRA"). In the Notice, the NCUA states that it is continuing its review of its regulations to identify outdated, unnecessary, or unduly burdensome on regulatory requirements imposed on federally-insured credit unions pursuant to EGRPRA.

The Notice requests comments and suggestions on ways to reduce burdens in regulations that govern Agency Programs, Capital, and Corporate Credit Unions, consistent with the NCUA's statutory obligations. Accordingly, U.S. Central respectfully offers the following suggestions.

Part 704.3 – Corporate Credit Union Capital

Part 704.3, which establishes the requirements for corporate credit union capital adequacy, is outdated in that it fails to adequately address to varying risk profiles of the existing array of corporate credit unions. Part 704.3's failure to measure the ratio of a corporate credit union's capital to its risk adjusted assets puts corporates out of the mainstream of all other depository institutions in America. This failure deprives both governmental bodies and the industry of a valuable tool to more precisely evaluate a corporate credit union's relative capital strength. Without this tool, the adequate capitalization of corporate credit unions has continually come into question. U.S. Central therefore urges the NCUA to consider the modernization of Part 704.3 to include the measurement of risk-based capital.

Part 704.5 – Investments

Among other things, Part 704.5 sets forth permitted investments and investment activities for corporate credit unions. As the NCUA is aware, the market for investment securities and investment activities is constantly evolving, with new vehicles being introduced almost daily. While Part 704.5 generally provides sufficient flexibility to permit corporate credit unions to prudently take advantage of appropriate vehicles, occasionally the regulation proves to be outdated and unduly burdensome because it fails to permit an investment or activity which either increases value without assuming undue risk or helps manage risk without unduly depressing value. One such instance is found in the case of investments that are linked to changes in indexes of inflation.

Consistent with its Part IV Expanded Authorities, U.S. Central uses derivatives transactions not only to manage its own balance sheet, but also to create structured products for its members and to assist it members in hedging their balance sheets. U.S. Central would like to create investment products for its member corporate credit unions by using interest rate swaps that are tied to changes in the Consumer Price Index, or some other inflation index ("inflation-linked instruments"). Whether and to what extent U.S. Central would require a modification of its own expanded authorities in order to purchase, hold, and dispose of inflation-linked instruments is not the subject of this letter. Rather, U.S. Central believes that Part 704.5 should be modified to allow corporates in general to purchase, hold, and dispose of inflation-linked instruments, subject to the other investment limitations of Part 704. If Part 704.5 were modified to permit corporate credit unions to purchase, hold, and dispose of inflation-linked instruments, they could obtain such instruments from U.S. Central or other market counterparties.

Inflation-linked instruments are widely available in the financial marketplace and, when used appropriately, are efficient, effective hedges against inflation in that they generate a return that exceeds the prevailing inflation rate by a specified amount. Inflation-linked instruments can add important diversification to a corporate credit union's investment portfolio. By providing returns that move differently from those of other assets, inflation-linked instruments can help reduce risk in a corporate credit union's entire investment portfolio.

Without the authority under Part 704.5 to invest in inflation-linked instruments, corporate credit unions are unduly burdened, competitively disadvantaged, and – most importantly – deprived of a valuable tool for interest rate risk mitigation. U.S. Central accordingly recommends that Part 704.5 be amended to permit corporate credit unions to invest in inflation-linked instruments.

Part 704.11 – Corporate Credit Union Service Organizations (Corporate CUSOs)

Definition of "Corporate CUSO"

Subpart (a) of Part 704.11 defines a "corporate CUSO" as an entity that:

(1) Is at least partly owned by a corporate credit union;
(2) Primarily serves credit unions;
(3) Restricts its services to those related to the normal course of business of credit unions; and
(4) Is structured as a corporation, limited liability company, or limited partnership under state law.

Part 704.11 then goes on to limit that activities of corporate CUSOs and to restrict the nature and extent of a corporate credit union's involvement with a corporate CUSO. U.S. Central believes that the vagueness of the phrase "at least partly owned" means that every entity in which a corporate credit union has a mere one dollar equity interest could be a corporate CUSO, subject to the limits and restrictions of Part 704.11. The broad application of this section could result in either unnecessarily burdensome restrictions and requirements on an entity in which a corporate credit union had a *de minimus* equity position or unfair restrictions on a corporate credit union's ability to take a modest equity stake in an otherwise worthwhile business entity.

U.S. Central respectfully recommends that Part 704.11 be amended to provide an exception from its restrictions and requirements in the case of an entity that is not controlled directly or indirectly by a corporate credit union. For this purpose, there might be a rebuttable presumption of "control" when a corporate credit union or group of corporate credit unions owned more than a certain percentage of the outstanding voting equity securities (*e.g.*, 20 percent) or had significant representation on the board of directors (*e.g.*, 20 percent or more of the seats).

Loan Limits to Corporate CUSOs

Subpart (b) of Part 704.11 is unduly burdensome in that it unnecessarily restricts the amounts that corporate credit unions may lend to member and nonmember corporate CUSOs. Currently, a corporate credit union is limited to extending 30 percent of its capital in investments in and unsecured loans to *all* corporate CUSOs, plus an additional 15 percent in secured loans to *all* corporate CUSOs. This is an aggregate limitation.

Meanwhile, under Part 704.7, (a) the maximum aggregate amount in *unsecured* loans and lines of credit to *any one member credit union* may be up to 50 percent of the corporate credit union's capital; and (b) the maximum aggregate amount in *secured* loans and lines of credit to any one member credit union may be up to 100 percent of the corporate credit union's capital. A corporate credit union with either Part I or Part II Expanded

Authorities may extend *unsecured* loans and lines of credit to any one member credit union up to 100 percent of the corporate credit union's capital.

Moreover, for all corporate credit unions, the maximum aggregate amount of loans and lines of credit to *any one other member* (other than a member credit union or a corporate CUSO) may be up to 15 percent of the corporate credit union's capital. The limit on a corporate credit union's authority to lend to non-credit union, non-corporate CUSO members is – effectively – limited only by the size of the corporate credit unions assets, while the same corporate credit union's authority to lend to all corporate CUSOs cannot exceed 45 percent of its capital, less any amount it has invested in all corporate CUSOs.

By comparison, therefore, corporate credit unions have far greater latitude to extend loans and lines of credit to all their other members than they have with respect to corporate CUSOs. Because U.S. Central can find no reasonable justification for this disparity, U.S. Central considers this limitation to be outdated and unduly burdensome. This is especially the case given the requirement of subpart (b) of Part 704.7 that a corporate credit union may only extend a loan to any borrower "after analyzing the financial and operational soundness of the borrower and the ability of the borrower to repay the loan."

U.S. Central accordingly recommends that Part 704.11 be amended to eliminate its separate loan limits and that loans to corporate CUSOs be made subject to the general limitations of Part 704.7.

Corporate CUSO Legal Opinion Requirement

Subpart (d)(1) of Part 704.11 requires that a "corporate CUSO be operated as an entity separate from a corporate credit union." Subpart 704.11(d)(2) goes on to require that a corporate "investing in or lending to a corporate CUSO must obtain a written legal opinion that concludes the corporate CUSO is organized and operated in a manner that the corporate credit union will not reasonably be held liable for the obligations of the corporate CUSO." The regulation even specifies what the corporate's legal counsel must address in the opinion, including "factors that have led courts to 'pierce the corporate veil,' such as inadequate capitalization, lack of corporate identity, common boards of directors and employees, control of one entity over another, and lack of separate books and records."

U.S. Central supports the goal of ensuring that corporates adequately address the legal risk potentially associated with investing in or lending to a corporate CUSO. However, the legal opinion requirement of subpart 704.11(d)(2) is outdated, unnecessary, unduly and burdensome, and it precludes reasonable operating flexibility and puts corporates at a competitive disadvantage. Moreover, no other insured depository institution regulated by any other FFIEC regulatory authority is subject to the same or a similar legal opinion requirement.

In the past 20 years, U.S. Central has invested in, or made loans to, six corporate CUSOs. During that period, there has not been a single claim threatened or asserted against any such corporate CUSO by any third party to the effect that such corporate CUSO was the alter ego of U.S. Central and that it would, therefore, be appropriate for a court to "pierce the corporate veil" between such corporate CUSO and U.S. Central. Further, where a corporate makes a loan in the ordinary course of business to a corporate CUSO in which the corporate has less than a controlling equity investment, it is extremely unlikely for a court to find that the borrowing corporate CUSO is the alter ego of the lending corporate. Both experience and legal principle demonstrate that corporates do not face any significant degree of legal risk associated with investing in and making loans to corporate CUSOs.

In addition, the regulation eliminates the ability of a corporate to assume and prudently manage what has proven to be a negligible legal risk. Corporates do not necessarily choose to invest in or make a loan to a corporate CUSO because they are seeking the limited liability that a separate legal entity may afford. In the case of all of U.S. Central's corporate CUSOs, limited liability is not the motivation at all. The principal motivation for operating a particular business unit as a corporate CUSO is, in every case, some legal, regulatory, tax, or business consideration *other than limiting legal liability.* Absent such other considerations, U.S. Central would operate each such business unit as a division of U.S. Central, where U.S. Central could and would clearly assume all the attendant legal risk. If a corporate otherwise would be willing to assume the legal risk associated with investing in or lending to a corporate CUSO (particularly in the case of a wholly- or majority-owned CUSO), that corporate should have the flexibility to forego the legal opinion requirement.

Therefore, the corporate CUSO legal opinion requirement is outdated, unnecessary, and unduly burdensome; it precludes reasonable operating flexibility and places corporates at a competitive disadvantage. U.S. Central accordingly recommends that subpart 704.11(d)(2) be eliminated, and that subpart 704.11(d)(1) be allowed to stand on its own.

Appendix B to Part 704 – Expanded Authorities and Requirements – Part V

Part V Expanded Authorities permit a corporate credit union that has met the applicable requirements to participate in loans with member natural person credit unions as approved by the Director of the Office of Corporate Credit Unions and subject to certain restrictions. This portion of Appendix B is outdated and unduly burdensome in that, as currently worded, it would not permit a wholesale corporate credit union to participate in a loan made by a non-member natural person credit union. Clarifying this authority would increase operating flexibility and improve lending efficiency, thereby enabling U.S. Central to assist the corporate credit union network in providing expanded loan and liquidity services to natural person credit unions. Without this clarification, Part V is outdated and unduly burdensome and U.S. Central, therefore, recommends that Part V be some amended.

Closing

Again, U.S. Central appreciates the opportunity to comment in response to the Notice. We hope that our comments will assist the NCUA in identifying outdated, unnecessary, or unduly burdens on regulatory requirements imposed on federally-insured credit unions pursuant to EGRPRA.

If you have any questions regarding the foregoing, or if you require additional information, please contact François G. Henriquez, II, U.S. Central's Senior Vice President and General Counsel, at fhenriquez@uscentral.org, or at 913-227-6035.

Respectfully,

Francis Lee
President and CEO